No. 14913.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

KEENAN PIPE & SUPPLY COMPANY, a corporation,
Appellant,

vs.

B. E. SHIELDS, as Trustee in Bankruptcy of James T. Inman,
Appellee.

APPELLANT'S REPLY BRIEF.

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TABLE OF AUTHORITIES CITED

Cases

Statutes

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In his brief appellee contends that all transfers within the four month period prior to bankruptcy (if the other elements are present) are voidable unless:

(1) There is a valid lien held by the transferee and that this lien must be on the property of the bankrupt; or

(2) That the transferee held a recognizable equitable lien against the property of the bankrupt.

In support of his contentions, appellee asks this Court to construe the provisions of Sections 60 and 67 of the Bankruptcy Act, and conclude that the only property to which the liens referred to in said Section 67 could attach are the properties of the bankrupt. On this issue appellant contends that the liens referred to in said Section 67 are not so limited but also extend to liens on properties other than those of the bankrupt. This is the holding of the case of *Jackson v. Flohr,* 119 Fed. Supp. 305

(decided after the effective date of the 1938 and 1950 changes in the Bankruptcy Act) in which the Court stated, *inter alia:*

> "Plaintiff would limit the mechanic's lien preference, made by reference in the Bankruptcy Act, to liens attaching to the property of the bankrupt. The Washington lien statute is not so limited and certainly Section 107, sub. b, of the Act, expresses no such limitation. To read such restriction into either the lien statute or Bankruptcy Act does violence to the spirit and language of both and vitiates the expressly granted preference to those entitled to lien status in a very substantial number of instances of great practical and commercial importance.
>
> "By the express terms of Section 107, sub. b, a mechanic's lien can be completed and enforced after bankruptcy adjudication without effecting an unlawful preference. If so, it surely could not have been the legislative intent that an unlawful preference result from satisfaction of a fully valid inchoate lien through payment of the debt secured by the lien prior to adjudication."

See also:

Cutler Hammer, Inc. v. Wayne, 101 F. 2d 823;

Perry v. Wood, Clerk of Court, 63 F. 2d 257.

Appellee recognizes that the *Jackson* case supports appellant's contentions but attempts to distinguish it by saying that the lien laws of Washington and California are different. As we read the cases the principal differences are that in Washington the materialman must, within five days of starting to deliver materials, give the owner written notice that he the materialman is so delivering materials and must record his claim of

lien within ninety days after his last delivery, while, on the other hand, in California no such notice to the owner is required and the materialman must record his claim of lien or file his stop notice within thirty days after recordation of Notice of Completion or within the prescribed period after cessation of labor. In both the *Jackson* and the present case the materialman had taken all steps required to be taken by law up to the date of payment. The Court held, in the *Jackson* case, that where such liens existed, payment and extinguishment of the lien within the four month period did not effect a preference. Appellee further attacks this case as being unsound but fails to point out wherein the decision is unsound.

It is appellant's contention that it held valid liens against the funds earmarked for the state project and on the properties on which the private residences were constructed; not on the bankrupt's alleged account receivable as contended by appellee.

Appellee cites the case of *Kruse v. Wilson,* 3 Cal. App. 91, to the effect that a materialman, by filing a stop notice with the contractor, cannot intercept money due from the contractor to the sub-contractor. Appellant takes no exception to this principle but it is suffice to note that appellant's stop notice rights (conceded by appellee) were against the funds in the hands of the public body pursuant to Section 1191.1 of the California Code of Civil Procedure not on any funds due from the contractor to the debtor.

Appellee as above noted treats the situation as one in which the bankrupt has transferred to appellant an account receivable; however, appellant contends that there was no transfer of a receivable by the debtor *but the extinguishment of valid liens by the general contractor.*

For the purpose of argument, let us assume that appellant filed its Stop Notice with the State of California and recorded its materialman's lien. If enforcement of such liens was effected by suit or otherwise, the monies due appellant therefrom would have been paid to appellant by the State or by the owner *and would never have become an asset of the debtor's estate nor would such payment have caused a depletion of his assets.* Can it then logically be said that payment by the general contractor, when faced with imminent prospect of Stop Notices being filed, of monies due a materialman holding valid liens, caused a depletion of the bankrupt's estate?

There is no conflict between the parties that Deeter paid out the monies to appellant in pursuance of their prior agreement, Deeter having stated that he had reimbursed himself for the amounts which he had advanced to meet the bankrupt's labor payrolls and that he felt that there was still sufficient money yet coming from the State of California to reimburse himself for the monies paid to appellant to satisfy its materialman's lien. Appellee concedes that the payment by Deeter to Keenan of the first check antedated the receipt of the balance of the money from the State of California. Thus the payment from Deeter to appellant must have been as testified by Deeter for Deeter's own account to extinguish the appellant's liens. There was ample consideration passing from appellant to Deeter for the said payment by Deeter. If Deeter, from monies normally due the bankrupt, subsequently reimbursed himself for the payment to appellant, should not the trustee look to Deeter to recover the preference, if any, that resulted from Deeter's action?

It should be noted that the monies here sought to be recovered from appellant were funds paid out by the gen-

eral contractor Deeter. The reason for making the larger of the two checks payable jointly to the bankrupt and to appellant was to obtain from the bankrupt an acquittal as to the amount of the payment and to prevent the bankrupt from seeking a double recovery from Deeter. The payment by Deeter was intended for appellant to extinguish its lien rights and was not the payment to the bankrupt of his account receivable.

Appellee apparently contends that if appellant had filed a stop notice and recorded claims of lien and thereafter received payment, no preference would result. Appellee finds fruition of the lien by filing stop notice or recording claim of lien. It is submitted that the liens existed and the filing of the stop notice or recording of claims of lien are only steps of enforcement of the existing liens and hence such filing or recording add nothing to the lien itself.

Conclusion.

Appellant respectfully urges that this Court determine that no preference results from the extinguishment of a materialman's lien by payment from the general contractor within the four month period prior to bankruptcy, and that the judgment appealed from is erroneous and should be reversed with direction to enter judgment in favor of appellant with costs.

Respectfully submitted,

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MARK WATTERSON,

Of Counsel.